Future Approaches to the Economic Instrument of Power

By PHILIP Y. KAO

Secretary Rumsfeld waves to tourists while meeting with civilian and defense officials in Beijing

1st Combat Camera Squadron (James Bowman)

COMMENTARY

We have no eternal allies and we have no perpetual enemies. Our interests are perpetual and eternal and those interests it is our duty to follow.

—Lord Palmerston, British Foreign Secretary, 1848

The U.S. military should capitalize on a greater understanding of economics. Indeed, identifying supporting relationships and how the military and key economic and financial figures interact may prove to be a daunting task, but it will enhance the strength and cohesiveness of national security. Whether it is gathering intelligence, providing security, shoring up market confidence, or supporting the execution of economic policies abroad, the military clearly has an economic function. By reinforcing geographic boundaries, the Armed Forces play an inevitable role in shaping local and regional labor markets. Additionally, the military is an enforcer of contracts, providing traction and realism to burgeoning rule of law and economic reforms, especially in the immediate postconflict environment.

The greater Department of Defense (DOD) community should incorporate economic analysis more prevalently into its planning consciousness and the various phases of operations. Prior to conflict, intelligence efforts conducted jointly by military and economic subject matter experts should discover local expressions of politics and economic relationships. Delineating these structural relationships will help situate and ground later cultural observations into a meaningful context. Moreover, a robust preconflict economic analysis needs to determine the risk preferences of a given country's government. To carry this out, analysts can scrutinize government investments and purchases and look for patterns of trade and regional economic behaviors. During conflict, economic assessment can not only draw on the prior knowledge base but also expand the horizon toward finding economic and resource leverage points and military financing mechanisms. Lastly, in the postconflict phase, economic reconstruction and development should seek to leverage the ongoing and cumulative dialogue between military and economic planners. Probing for real economic capacity on the ground is vital and can thwart a premature and headlong dive into yet another gargantuan institution-building campaign.

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Defense academics and thinkers have turned a closer eye to social and cultural knowledge since the threat of terrorism took center stage post-9/11. Research conferences sponsored by think tanks and blossoming journal publications have attempted to extract military and security insight from such fields as cultural anthropology and sociology. Along with this renewed focus on "social factors," research and development pouring into complex systems modeling has given planners guidance and probability tools for analyzing and conducting counterterrorist and counterinsurgency operations.

One discipline, economics, which has been (in)famously called "the dismal science" for its cold-hearted and scientific analysis, has been slowly withdrawing behind the curtain. Once the darling child of the post–Cold War era, economics is now coming close to the limits of market fundamentalism and exhausting its own ideological circumlocution. Contrary to public opinion, there was a postconflict plan in Iraq, and it echoed the millennial slogan, "It's the economy, stupid!" Naomi Klein offers the poignant observation that injecting greed and free-market economic shock therapy into Iraq was indeed a failure and contributed to the escalation of Iraqi insurgency.[1]

Economists often ostracize their readers by presenting a deterministic conception of the world. This article, however, steers economics back into our military knowledge base and suggests that failure to do so could be highly detrimental, given the nature of future threats.

Analyses of a Working Partnership

DOD frequently treats economics as a shorthand for macromovements of cash

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flows. This approach is highly superficial and more in line with accounting than the actual science of economics and its various applications. Additionally, the media tend to focus on economics when hand-wringing over the financial and opportunity costs associated with war. For the future, however, we need to deepen our awareness of economics beyond these wave-top representations. The need to share information across U.S. agencies will be paramount in the years to come. Achieving a harmonized, government-wide effort will become the dominant business practice. Unified action is one such concept gaining a second life in this milieu, which harnesses multiple Federal departments and agencies to carry out national strategy directives more efficiently and effectively.

Under this framework, the growing need for economic experts and planners to weigh in critically on the consequences of military action will only intensify. Economics can inform policy instrument options (for example, incentives and sanctions) to prevent kinetic wars or even to terminate conflict midstream without sacrificing our strategic goals. Flexible deterrent options are not new to the military community, and surely they make up certain courses of action in strategic theater cooperation planning, albeit rather anemically.


1st Combat Camera Squadron (Jason Bailey)

U.S. Army engineer reviews plans for clinic with Iraqi contractors

What is new, however, is the need to reach beyond DOD and tap outside subject matter experts in various other departments and agencies as working partners. Military planners need to learn more about how they can tailor their interventions, teeing up for a sustainable phase of economic reconstruction. Battle damage assessments of diplomatic channels of strategic communication, economic drivers of growth, trade, and commodity chain networks are just a few examples of the kinds of analyses a working partnership could conduct.

Ultimately, economic actions may prove more palatable in the international arena than unilateral military interventions. Japan is an example. In light of Article IX of its constitution, Japan engages in political realism through the pursuit of economic power. As Samuel Huntington asserts, "In the realm of military competition, the instruments of power are missiles, planes, [etc.]. In the realm of economic competition, the instruments of power are productivity, market control, trade surplus, strong currency, foreign exchange reserves, ownership of foreign companies, and technology."[2] By raising our consciousness and appreciation of economics, we can create better national security options and results.

Policy Schizophrenia

In the past, economics and national security shared traditional and overlapping concerns. Robust growth and economic welfare were keys to securing a Maslowian-inflected hierarchy of needs. According to Aharon Barth, the economy is an integral part of military capabilities, such as maintaining a healthy industrial-military complex.[3] Also, Barth maintains that in the interconnected global economy, a nation-state's position within the interdependent network presents itself as a double-edged sword—that is, as a simultaneous instance of power and vulnerability. These concerns are still extremely valid, but other economic strands of thinking and relating must be showcased as well.

U.S. foreign policy orientation to economics has always been rather schizophrenic. During the Cold War, policymakers wanted failing and weak states to grow economically in the hopes of spreading liberal democracy. Military and "social systems" analysts paid extraordinary attention to the causes of civil wars. Indeed, this fixation on failing states and underperforming economies continued through the fall of the Soviet Union. Under the aegis of the post–Washington Consensus, transparency, accountability, privatization, and liberal democracy were packaged into a sacred bundle and parachuted into "unclean" developing countries. Simultaneously, however, policymakers have remained threatened by competitive economies, despite their market leanings. In other words, we have a publicly contradictory policy that extends the olive branch of trade and liberalism while simultaneously refusing to sell certain assets to foreign countries in the name of national security. This economic dilemma is certainly rhetorical and attributable to our (sometimes) polarized political theories that hedge outspoken liberalism with Kissinger-style realism.

Policy articulations of economics are bifurcated along two strands of political thought. On the one hand, policies drawing from the doctrine of economic liberalism are called on to quell erupting civil wars and nascent insurgencies abroad, especially in areas that have been referred to as the *nonintegrating gap*.[4] Liberalism stems from the rationale that economic well-being and exchange promote complacency, mutual understanding, and risk-averse behavior. On the other hand, an honest engagement with economics must face up to the (realist) question: How do we go to war and dominate someone who is becoming more economically intertwined with us?

Paul Collier, the former director of research at the World Bank, started a wave of investigations into the economic relationships arising out of the world's messy conflicts after World War II.[5] Working with a large dataset, he ascertained some statistically significant relationships, including the observation that economic greed, corruption, and a disproportionate ratio of natural resource export income to gross domestic product are all correlated with conflict. His thesis jumpstarted an academic reaction within the development community because it suggested that greed, rather than political grievance, motivates and sustains civil wars and conflicts. Collier also concluded that peacetime corruption probably has a strong link to economically motivated conflict and that the longer a war lasts, the more likely violence will become economically motivated.

These claims beg for an understanding of how our actions, either by the military or a civilian-military coalition, reproduce the conditions and terms of violence and cause conflicts to relapse. Development academics argue that the law of diminishing returns applies to foreign direct investment and aid. Perhaps there are military actions with diminishing returns and elasticities that we need to identify and put on the table.

The Liberalism/Realism Debate

Economic reconstruction is too often caught up in postconflict planning and should be embedded more thoroughly in military planning. Keeping a blind eye to corruption and informal markets may be politically expedient, especially during the drafting of a peace agreement. Common sense, however, suggests otherwise. Informal economies are not only dangerous breeding grounds for illicit trade but, more importantly, are also incapable of mobilizing resources (raising taxes) for investing in the public good. Failure to generate and spread prosperity will lead to future conflicts and instability. This brings us to the point that economics and conflict are not so distinct. David Keen, for example, writes that war should not be perceived as an outgrowth of chaos theory, where violence signals a massive societal meltdown. "Rather," he states, "conflict and war is simply a break of a particular system in the hopes of creating an alternative system of profit, power, and even protection."[6]

Unlike liberalism, realism postulates that nation-states are rational actors looking to maximize security gains. Realists argue that economic growth enables nation-states to develop stronger military capabilities and that actors are more willing to engage in war today to secure a higher position tomorrow. Realism also posits that nation-states will leverage their economic powers to influence and threaten those who are weaker. With the epigraph from Lord Palmerston in mind, determining clear-cut friends and foes will be increasingly difficult, especially in economic interdependence. One has to be clear, nonetheless, that economic growth and market-led reforms do not always coincide with Western democratic reforms; they are not hand-in-glove issues. Growing economies may exhibit increased nationalism and clamor for conspicuous cultural politics that, in the best-case scenario, act as an alternative to "our" models and at worst as an antagonistic competitor. There is a dire need to find ways of dissuading growing economies from investing in defense. (Over)investment in a military may give regional neighbors the wrong security signals, prompting a regional arms race. More importantly, if these countries experience significant economic downturns, they will be left with stockpiles of weapons as their only international bargaining chips.

Research of economic interdependence can take some cues from models arising out of the Palestinian-Israeli case study. Gil Friedman conducted a brilliant analysis that explored the impact of economic incentives on views of peace and violence.[7] His study, a regression model of Palestinian views on diplomacy and attacks using 2001 public opinion data, is couched broadly around the liberalism/realism debate. Friedman suggests that there is a modest role for economics, and he tests three hypotheses that state, in summary, that mutually beneficial transnational exchange (between Israel and Palestine) reduces the utility of warfare, enriches the nations, and thereby engenders a preference for the status quo, promoting a positive effect. He concludes that for those who view economic improvement as the most important factor, there is a strong correlation between economic integration and support for peaceful diplomacy. On the other hand, respondents who did not view economic improvement as the most important issue tended to support attacks against Israel even when they believed it damaged the economy. Perhaps the greatest conclusion, and a rather subtle one, is what Friedman describes as Hypothesis 4:

The salience of economic concerns relative to other concerns modifies the strength of the relationship between economic motives and views on war and peace. One way forward could be to conduct similar research but into different areas and relationships.

A Shift in Thinking

There are some tangible economic policy instruments and overall directions to take in boosting our national security and strategic capabilities. First, policymakers should avoid meddling with monetary policy. Our currency and economic strengths trade off of growth and return-on-investment opportunities. Synchronizing interest rates and money supply with national defense strategy would signal a moral hazard and weaken our position in the global economy. With that said, sanctions provide a feasible solution, albeit imperfect in many situations. Critics of these policies argue that sanctions fail because they create subterranean informal markets. Examples of relatively successful sanctions such as the Kimberley (diamond) Process demand a closer study. Alternatively, creating a two-tier market system that makes the cost of business unsustainable for informal market entrepreneurs is one way to deal with informal markets.

> economic role playing should be elevated at military exercises and given life outside of the closeted world of wargaming

Staying economically competitive allows us to manufacture favorable tradeoffs. For example, China has recently traded in its political relationship with North Korea for future investment and trade opportunities with the United States. Innovating and creating new market niches should ensure our continued economic dominance, diminishing the impact of outsourcing. Without transgressing international dumping laws, new cost-effective ways of pushing out exports and raising tariffs on select imports will be useful yet limited tools. Furthermore, research should explore the feasibility of creating market panics and financial crises. How could we overinvest deliberately in a region in order to induce capital flight, distort regional markets, and create future levers of power? The economics of the information subdiscipline also offers promising insight. Are we hurting our future prospects by ceding away too much in the way of technological and knowledge capital transfers? In other words, is there an unfair arbitrage that is leaving us short-changed? The devil is in the details, and there needs to be an examination of the timing and sequencing of such economic actions alongside other national government strategies.

Interdependence entails a certain shift in thinking about foreign investments. Going along with the conventional wisdom that it is always better to wage war on someone else's turf, we need to consider the types of investment and capital we risk losing in foreign countries during conflict. One hedging strategy is to tilt foreign investments toward mobile assets such as knowledge and human capital; these would be recoverable sunken costs during times of war. As a corollary, we need to make sure that foreign investments in the United States can be replaced relatively cheaply or substituted away.

Under the liberalist framework, economic policy instruments look rather different. For one thing, information operations (IO) present a commonsensical opportunity for military planners and economists to collaborate. Promoting economic growth and spreading awareness of economic empowerment functions as an effective counterinsurgency tactic. In addition to buying away spoilers, IO campaigns that draw from economics can plant the seeds of self-empowerment, democratic participation, and civil society. The increasing debt of the developing world may be a source of violent tension, but

55th Signal Company (Charles Gill)

there are opportunities as well. Tied aid and debt forgiveness are implicated in a system of rewards and political reform.

To facilitate a working dialogue between economics and national security, we must be willing to transform. Military planners and strategists must appreciate the sensitivities surrounding the reluctance on the part of many professional economists to participate in discussions spanning economics and national strategy. For one thing, "applied" policy economics is entrenched in normative struggles to solve the woes of underdeveloped countries. Development economics proceeds from understanding economics as a science of maximization, concerned with crafting efficient solutions to situations where the lack of resources threatens to undermine rational behavior and distribution. In a nutshell, normative economics in practice concerns itself with maximizing the greatest good for the greatest number of people. Additionally, economists fear that treating their discipline as a weapon vitiates the unfettered nature of the market system and generates distorting price and information noise. For these academics, war is an exogenous shock and signifies points along a historical time-series. Keeping aware of these normative and institutional tendencies will help pave the road toward effective communication techniques that will bolster the overall national security dialogue.

Economic Relationships as Enablers

The military planning and research community should wean itself away from conventional diplomatic, information, military, and economic (DIME) analysis. Instead of being just a convenient mnemonic for getting planners to think holistically, there is a growing danger that DIME is ossifying our thinking with respect to social analysis. Too many people eschew various models because the models force them to identify an action or effect solely in terms of DIME-generated categories. One of the powerful conclusions coming out of Collier's research is that conflict is triggered by the interaction of economic motives and other factors such as social and cultural politics. Economic relationships, just as any other cultural or political observations, are really enablers among social variables. The way they play out is always contingent on the dynamics of each situation. To treat economics rigidly within the framework of DIME would amount to a certain degree of negative training.

To deepen our understanding and move away from a superficial DIME analysis of economics, military training needs to venture into such topic areas as new institutional economics, different markets' ontologies, behaviors, and the forces and types of capital that regulate preferences and clear imperfect contracts.[8] Complementary to all this, economic role playing should be elevated at military exercises and given life outside of the closeted world of wargaming. Having various economists (representing the Department of the Treasury and the Federal Reserve, for example) train and adjudicate options under pressurized situations within a command post exercise would be highly valuable.

People often refer to the economic instruments of power as the carrots and sticks. But we need a sophisticated and coordinated national security strategy that differentiates when and where the Nation is promoting economic cooperation/growth versus protecting itself from the vulnerabilities inherent in interdependence. Allowing slippery language to infect policy will lead to disastrous confusion. Being explicit about our strategy and economic instruments will help us remain flexible and shuffle between liberal and realist positions with lower transition costs. An economist at U.S. Joint Forces Command claims that in times of peace, we need to harness the U.S. Government to persuade, influence, assist, reward, and socialize. In times of conflict and crisis, he suggests looking for "unified economic actions" to dissuade, deter, isolate, defeat, and dominate. These economic carrots and sticks should be indexed more explicitly to strategy and political goals, regardless of whether there is peace or outright war. **JFQ**

NOTES

[1] Naomi Klein, "Baghdad Year Zero," *Harper's* 309, no. 1852 (September 2004), 43–53.

[2] Samuel P. Huntington, "Why International Primacy Matters," *International Security* 17, no. 4 (Spring 1993), 73.

[3] Aharon Barth, "Econo-Realism: Putting Economics at Center Stage. How Does, and Should, IR Research React to Expanding Economic Interdependence?" paper presented to the International Studies Association 41st Annual Convention, Los Angeles, March 14–18, 2000, available at <www.ciaonet.org/isa/baa01/>.

[4] Thomas P.M. Barnett, *The Pentagon's New Map* (New York: Putnam, 2004).

[5] Paul Collier, "Development and Conflict," Centre for the Study of African Economies, Department of Economics, Oxford University, October 1, 2004, available at <www.un.org/esa/documents/Development.and.Conflict2.pdf>. See also Paul Collier and Anke Hoeffler, "Greed and Grievance in Civil War," *Oxford Economic Papers 2004* 56, no. 4, 563–595.

[6] David Keen, *The Economic Functions of Violence in Civil Wars*, Adelphi Paper 320 (New York: Oxford University Press for the International Institute for Strategic Studies, 1998), 11.

[7] Gil Friedman, "Commercial Pacifism and Protracted Conflict: Models from the Palestinian-Israeli Case," *Journal of Conflict Resolution* 49, no. 3 (June 2005), 360–382.

[8] See Samuel Bowles, "Endogenous Preferences: The Cultural Consequences of Markets and Other Economic Institutions," *Journal of Economic Literature* 36 (1998), 11; and Samuel Bowles, *Microeconomics: Behavior, Institutions and Evolution* (Princeton: Princeton University Press, 2004).

COMMENTARY